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1983/01/27



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United States Department of State

Washington, D. C. 20520

79

BRIEFING MEMORANDUM
S/S

January 27, 1983

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TO: The Secretary
FROM: EA - Paul Wolfowitz
SUBJECT: Your Meeting with Jia Shi, Vice Minister of Foreign Economic Relations and Trade

I. YOUR OBJECTIVES

1. Comment briefly about global economy and stress value of Chinese involvement (Talking Points attached).
2. Review US-China economic relations. Outline areas for growth in trade, including services. Encourage diversification of PRC exports (Talking Points attached).
3. Stress need for a secure environment for investors, including bilateral agreements and a Chinese patent law; briefly address textiles issue; address high technology and US export licensing; seek Chinese respect for U.S. laws (Talking Points attached).
4. Raise problems of poor Chinese performance under our maritime agreement (Talking Points attached).
5. (Contingency) Respond to specific criticisms of US trade practices (Talking Points attached).

II. SETTING

The Ministry of Foreign Economic Relations and Trade (MFERT) was established last March, as an amalgamation of four former departments. Jia is a Vice Minister (Chen Muhua, who became Minister in March 1982, is out of the country). Jia is familiar with US trade and visited the US for the first time for the December Joint Economic Commission meeting. He is an old member of the foreign trade establishment. Before the creation of MFERT, he was a Vice Minister of Foreign Trade. You should use your meeting with Finance Minister Wang Bingqian to emphasize the global economy and financial issues. With Jia, you should focus on trade issues.

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- 2 -

Before 1979, China's former Ministry of Foreign Trade rigidly controlled pricing, contracts, and access to enterprises by foreigners. By 1981, provinces and ministries, and even some factories, were allowed to deal directly with foreigners. This gave increased access for US business to Chinese enterprises and led to increased competition between those enterprises, which benefited our businessmen. However, the increased competition threatened the powers of the Ministry; and the lack of central control exacerbated problems involving exports to the US in sensitive areas because local trading corporations shipped without restraint. In 1982, MFERT began to take back some control. This has the beneficial effect of better regulating supplies and ensuring adherence to agreements. Yet it also had the negative effects of reinserting the central government into negotiations, limiting access to producers, and raising some prices.

Jia can be expected to criticize the trade imbalance and U.S. import and export restrictions. The breakdown of the textile negotiations this month will make the discussion of U.S. protectionism all the stronger. Our Embassy will have recently responded to Jia about a list of 30 problem export license cases and he may have a further list or more questions. He should be interested in trade prospects and areas for industrial cooperation.

III. PARTICIPANTS

US

The Secretary
Ambassador Hummel
EA - Paul Wolfowitz
PA - John Hughes
PM - Jonathan Howe
S - Raymond Seitz
NSC - Gaston Sigur
EA - Thomas Shoesmith
DOD - Richard Armitage
Embassy, DCM Charles Freeman
EA/C - William F. Rope
Economic Counselor David Brown
Commercial Counselor Mel Searls
Two Embassy language officer notetakers
Vivian Chang (Interpreter)

CHINESE

Jia Shi, Vice-Minister
Li Shude, Chief of American
Section

IV. Press Arrangements

Photo opportunity at beginning of meeting

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- 3 -

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1/26/83 X-22656

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EB/Tex:MHenderson (sub)

EB:RGold

EB/OMA:GBrown

Commerce:RPerito

EA:TPShoesmith

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- 4 -

V. OBJECTIVES

Comment briefly about global economic problems and value of Chinese involvement.

Jia may not be well prepared to discuss the global economy, but it would be useful to begin with a brief exposition of the current global economic situation.

-- World going through difficult time of transition from high inflation to stable growth--difficult because involves retrenchment in West, which has been motor of global economy.

-- Under current conditions, world trade declining. Many countries taking steps to protect markets. We trying hard to resist trend, though we too have had to make some adjustments.

-- We have stressed putting own house in order, because believe will enable us, in long term, to make sustainable contribution to world growth. President has taken steps to encourage savings/investment, lower inflation, lower interest rates, and achieve economic stability.

-- We also working with other developed nations to strengthen international trading system, through GATT in particular, and to take steps stabilize debt situation of many developing nations through stronger IMF.

-- China playing constructive role in multilateral financial organizations. Welcome this. Responsible Chinese participation in world economy not only helps your own economy but contributes to durability of institutions.

-- You have been an observer in GATT. Would be interested in your thoughts about membership.

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- 5 -

Review US-China economic relations. Outline areas for growth, including services. Encourage diversification of PRC exports.

	1980	1981	1982 (est.)
US Exports	\$3.7 billion	\$3.6 billion	\$3 billion
US Imports	\$1.1 billion	\$1.9 billion	\$2.3 billion
US Surplus	\$2.6 billion	\$1.7 billion	\$700 million

US-China trade grew from virtually nothing to \$5.5 billion in the first decade of US-China rapprochement (Chinese figures differ dramatically from ours). We have consistently recorded large merchandise surpluses, although, as shown in the figures above, the surplus is declining. In invisibles, the Chinese are ahead. Our Embassy estimates that in 1981 we had a \$500 million deficit in invisible trade with the Chinese--largely a result of remittances, tourism, and shipping.

In the decade ahead, agricultural products will continue to be a large component of our exports, but we will move into China's oil sector. Other major energy and mining projects, transfer of industrial know-how and continued sales of high technology will boost our exports. On the import side, we will continue to buy a wide variety of light industrial goods, plus petroleum based products; but Chinese exports of raw materials, chemicals, and machinery will grow. We need to encourage diversification, managed in a way that avoids market disruption.

-- Expansion in our trade remarkable. You now our 14th largest trading partner, we your third largest. Former President Nixon and General Secretary Hu Yaobang have proposed shoot for level of trade of \$50 billion or more by end of century.

-- US will continue as reliable supplier of agricultural products, especially grain, to China. Can also provide timber and paper products for Chinese industry.

-- Look forward to offshore oil and energy cooperation. U.S. firms can provide drilling/mining equipment; technical services; financial backing; transportation and construction equipment; know-how and managerial expertise for large infrastructure projects.

-- American manufacturing equipment can help modernize factories. U.S. firms can contribute feasibility studies, management consulting, banking services to help use potential effectively.

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- 6 -

-- We greatly benefit from wide range Chinese goods entering US market. Have imported Chinese bauxite for strategic stockpiles; Chinese components for US products such as airplanes and railroad engines. Chinese exports of raw materials, chemicals, and machinery will grow. Want encourage this diversification of trade.

-- U.S. by far one of most open/accessible markets in world. Even we, however, have import sensitive areas and forced limit imports in certain sectors affected by economic difficulties.

-- As your exports grow, hope you make effort to grow steadily, in stable manner. Extreme surges in shipments to US lead to domestic problems on our side which sometimes hard to contain.

-- Indeed, trade complaints have arisen, as you know, though we believe there are adequate mechanisms to ensure such cases decided fairly according to objective criteria.

-- Important work broaden understanding of respective market conditions. May wish to exchange delegations to discuss legal environments in China and U.S. or to plan marketing studies that would help increase trade in steady manner. These are subjects that could be explored further during Joint Economic Commission on Commerce and Trade meeting Minister Che will chair with Secretary Baldrige in May.

-- U.S. capital markets also open to China. Export-Import Bank and other government programs able to finance some projects; indeed our willingness to make good on Mondale's 197 commitment to make available \$2 billion Eximbank credit over five years remains unchanged; but, bulk China's foreign financing must come from private markets. We encourage you study and make use of financial markets. Interest rates have decreased recently, projects with solid rates of return should find financing easily.

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- 7 -

Briefly address textiles issue; stress need for a secure environment for investors, including bilateral agreements and a Chinese patent law; address high technology and US export licensing; seek Chinese respect for U.S. laws.

We have prepared a separate memo on the textiles issues. The talking points are repeated here.

US investment in China comes to about \$300 million. Opportunities for a substantial increase are present, but bureaucratic red-tape, legal ambiguities, and other factors have kept US investment from reaching its potential.

Textiles

-- Would like reiterate our sincere desire continue addressing textile trade problem through mutually acceptable agreement. Despite no agreement to date, we remain optimistic that a solution is attainable.

-- Naturally, like you, we disappointed that five months of negotiations failed produce new agreement. Want to reassure we do want agreement.

-- (If appropriate) We regret recent Chinese decision to limit purchases of cotton, chemical fiber, and soybeans. These restrictions undermine the spirit of constructive cooperation embodied in the trade agreement. We strongly believe that such retaliatory trade actions do not contribute to an atmosphere conducive to a mutually satisfactory settlement.

-- I wish stress our ability to be forthcoming is limited by difficult domestic conditions. U.S. textile and apparel industries hard hit.

-- Although U.S. domestic textile production has been declining in recent years, textile imports from China have grown 40% in 1980, 73% in 1981 and 19% in 1982. With such tremendous growth in recent years, you have now become our fourth largest supplier. By end this decade, you likely become our number one supplier.

-- These are very difficult problems involving both domestic considerations of jobs and recovery and international questions such as obligations to other suppliers. Must devote efforts to solving them and building stable long-term relationship where such issues are handled more routinely.

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- 8 -

-- I would like to assure you that we are prepared to resume negotiations at a mutually convenient date.

Investment Climate

-- We recognize and appreciate improvement in operating conditions for U.S. firms in China. But hope you continue devote great attention and efforts, further improvements in these areas.

-- Investors also need know assets and proprietary information protected. Comprehensive Chinese patent law needed to provide protection.

-- Our countries will begin negotiating bilateral investment treaty second quarter this year. Conclusion is important element to create proper environment for investment.

-- Discussion of investments often long and drawn out process. Time and effort spent by one firm on unproductive projects can frighten off others who interested. Need your help to streamline.

Technology Transfer

-- As our relationship has developed, there has been a steady expansion in trade of equipment and processes embodying dual-use technology.

-- Technology transfer also occurs through many other means: students, scholars, and trainees exchange ideas; management training; feasibility studies; etc. These all part of broad process of technology transfer which has begun between our two countries.

-- Many firms have expended much effort to inform Chinese end-users about products. In many cases, efforts not reciprocated, often no contracts have resulted.

-- Successful cooperation will depend on efforts of both sides to make good use of what already available. Bulk of equipment and know-how useful for development is available to China without restrictions.

-- Must note that we apply some restrictions on technology transfer in areas required for legitimate reasons of national security.

-- Restrictions apply only highest range of technology, and only technologies with direct and significant military applications.

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- 9 -

-- Secretary Haig, during his visit in 1981, informed you of President Reagan's decision to "significantly liberalize" licensing. Have done so.

-- Since 1979, license approvals up by 300%. Last year over 1700 export licenses approved for China. Great deal of what approved is state-of-the-art.

-- Can provide you with numbers/citations which show increase. But should look beyond numbers, focus on what both can do to improve technical cooperation between our countries.

-- Must speak frankly on one important point. Our export licensing laws must be respected. We receiving reports that Chinese entities are acquiring advanced equipment without proper licensing and that equipment sold to one end-user sometimes diverted elsewhere.

-- These activities make more difficult for us to move forward with new initiatives in this area and undermine atmosphere of trust we attempting to build.

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- 10 -

Raise problems of poor Chinese performance under our maritime agreement.

The 1980 US-PRC Maritime Agreement will expire this September and we anticipate difficulties in negotiating a successor. The heart of the 1980 Agreement provides a trade-off between expanded port access for the Chinese (although under restrictions which only apply to communist vessels) in exchange for a guaranteed one-third cargo share for the US. US ships carried only 14% of the liner cargo in the first half of 1982, and an insignificant portion of the bulk cargo.

Chinese cargo allocation is controlled by the Ministry of Communications and by MFERT. It is within their power to provide us the one-third share. We expect the Chinese to seek further liberalization of port entry and regulatory requirements in renewal negotiations, but we will not give it if they do not meet their commitments. We have invited a Chinese delegation to Washington in March for further talks.

-- Implementation of maritime agreement not satisfactory. Your ministries control allocation of cargoes; so long as they do, this will be governmental, not purely economic, problem.

-- Also delays and unusual fees associated with shipping from China have already raised costs of Chinese goods to our importers above those incurred in other countries.

-- These problems aggravate basic difficulty of cargo allocation. Maritime Agreement provides one-third cargo share for US vessels. This goal not been met.

-- Understand desire easier port access in United States. However, difficult for US side to offer increased access unless provisions of present agreement fully implemented.

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- 11 -

(Contingency) Respond to specific criticisms of US policy.

World Bank Oil Projects

The US voted against World Bank loans for the Daqing oil project in a World Bank meeting on January 25 because we believe the projects could find commercial financing. The negative vote was consistent with our votes against similar projects in India, and abstentions on projects in the Ivory Coast and Peru. The US was the only country which did not support those loans.

-- We believe funds for multilateral banks best used where private financing not available. China in excellent position to obtain private financing for oil development.

-- US cast similar votes on projects in India, Ivory Coast, and Peru. Have not singled out China.

Most Favored Nation Treatment

The Chinese cite the most favored nation principle not only for customs procedures and taxes, but also when speaking of shipping and other matters.

-- Most favored nation principle is special concept which governs trade and customs treatment. Other areas (export controls, maritime relations, civil aviation, investment relations) must be covered by agreements based on different principles. Is normal international practice.

General System of Preferences

-- Under our law, China not legally eligible for GSP program because not member of GATT. In line with policies conveyed to you by Secretary Haig to remove China from discriminatory legislation, another provision about world communist movement does not apply to China.

Sensitive US Industries and Unfair Trade Actions

China's non-market economy makes it an inviting target for market disruption, anti-dumping, or subsidy petitions. Zheng may ask what exports are likely targets.

-- China has taken steps to protect some domestic industries with tariffs, local preference requirements, other measures.

-- Several industries in U.S. currently feel threatened by Chinese imports. Growing reports of action which our industries might initiate against imports of manhole covers, steel nails, jewelry, cutting tools, footwear and tungsten products.

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- 12 -

-- If I can assure these industries--particularly tungsten products producers--that China intends to avoid increasing its high levels of exports during current recession, industries may choose not to file formal complaint requesting import restrictions.

Hukuang Railway Bonds

In September, a Federal court in Alabama entered a default judgment against the PRC for \$41.3 million due on bonds issued by the Imperial government in 1911. China refused to appear in court, arguing that it was immune to the jurisdiction of US courts and that it was not liable for the obligations of the Imperial government. A negotiated solution, recently suggested to the Chinese, could be based on principles of equity for the bondholders.

-- Another example of problems that arise as trade relations expand is question of liability for bonds that financed construction of Hukuang railway.

-- Do not wish this issue to disrupt trade relations. We believe negotiated solution would not compromise principles of sovereignty you maintain. Hope you will promptly pursue resolution of problem. Our Embassy can discuss this further.

Legislative Initiatives

During his visit in June 1981, Secretary Haig informed the Chinese, on behalf of the President, that the U.S. would seek legislative change to laws which lumped China with the Soviet bloc and which were not consistent with our present strategic relationship. Subsequently, we identified legislation inhibiting relations with China and submitted proposals to Congress urging the elimination of such restrictions (we did not seek to amend laws impacting on China if they had an economic basis, e.g. GSP).

-- In June 1981 trip to China, Haig stated U.S. would seek appropriate action to end past discrimination against China due to earlier association with Soviet bloc, and which is inconsistent with present strategic relationship.

-- Have been successful in clarifying and removing restriction on PL-480 assistance for China. In addition, President just recently signed (January 12, 1983) legislation lifting prohibition on importation of Chinese furskins.

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- 13 -

-- Proposal to eliminate prohibition of foreign assistance to China submitted to Congress last year in FY 83 foreign aid authorization bill; received favorable consideration in Senate Foreign Relations and House Foreign Affairs Committees. However, overall bill not passed in 97th Congress (reasons not related to China). Plan to resubmit proposal in FY 84 foreign aid bill.

-- (If Raised) Until legislative restrictions properly and fully addressed, is premature to talk about types of programs we might be able to offer China. Have stated to Congress that, if legislation passes, we intend to allow China to participate in ongoing, cooperative programs (e.g. agricultural research, S&T programs), under current funding levels, on same basis as other countries. For foreseeable future, with budgetary stringency, we do not envision direct aid programs.

-- (Follow-up to above if raised issue) In meantime, we pleased China able to benefit from Trade and Development Program, which helped finance, for example, exchange of experts under US-China Hydropower Protocol.

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